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No. _____

IN THE SUPREME COURT OF THE UNITED STATES

October Term 1988

PATRICIA B. TAYLOR, Petitioner,

versus

FIRST UNION CORPORATION OF SOUTH CAROLINA [FORMERLY SOUTHERN BANCORPORATION, INC.], *et al.*

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

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10 pp

QUESTIONS PRESENTED

1. Where defendants' fraudulent activities precipitate the plaintiff's sale of a security, can it be said that, as a matter of law, defendants' fraud is not "in connection" with plaintiff's sale within the coverage of Rule 10b-5?

2. Is a conspiracy to defraud an investor in connection with her sale of stock actionable under Rule 10b-5?

3. In the face of a jury verdict for a plaintiff selling shareholder, is nondisclosure that the company purchasing the shareholder's stock has become "pinned" to the issuer, preparatory to later acquisition, neither material nor misleading as a matter of law where, prior to the sale, the issuer's securities counsel, speaking on behalf of the issuer, notified the buying company that the issuer believed disclosure of the "pinning" was required by the securities laws?

LIST OF PARTIES

The parties to the proceedings below were petitioner Patricia B. Taylor and the respondents, First Union Corporation of South Carolina [formerly Southern Bancorporation, Inc.] and First Union Corporation.

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IN THE SUPREME COURT OF THE UNITED STATES

October Term 1988

PATRICIA B. TAYLOR, Petitioner,

versus

FIRST UNION CORPORATION OF SOUTH CAROLINA [FORMERLY SOUTHERN BANCORPORATION, INC.], *et al.*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The petitioner Patricia B. Taylor respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit, entered in the above-entitled proceeding on September 22, 1988.

OPINIONS BELOW

The opinion of the Court of Appeals from the Fourth Circuit is reported at 857 F.2d 240, and is reprinted in the Appendix hereto, p. 1a, *infra.* The order of the United States District Court for the District of Columbia (Ross Anderson, D.J.) has not been reported. It is reprinted in the appendix hereto, p. 13a, *infra.* The Fourth Circuit's Order denying the Petition for Rehearing with suggestion for Rehearing In Banc is reprinted in the Appendix hereto, p. 19a, *infra.*

JURISDICTION

Invoking jurisdiction under section 27 of the Securities Exchange Act, 15 U.S.C. § 78aa, petitioner brought this suit

in the District Court for South Carolina. On November 11, 1987, the jury returned verdicts against both defendants on plaintiff's count alleging a violation of Rule 10b-5, 17 C.F.R. § 240.10b-5, and on the count alleging a corporate breach of fiduciary duty to a minority shareholder. On December 28, 1987, the District Court denied respondents' motions for judgment notwithstanding the verdict and in the alternative for a new trial. See p. 13a, *infra*.

On respondents' appeal, the Fourth Circuit on September 22, 1988, entered a judgment and an opinion reversing the judgment entered below. A petition for rehearing was filed and was denied by the Fourth Circuit on October 21, 1988. See p. 19a, *infra*.

The jurisdiction of this Court to review the judgment of the Fourth Circuit is invoked under 28 U.S.C. § 1254(1).

STATUTE AND REGULATION INVOLVED

15 U.S.C. § 78j(b). Regulation of Manipulative and Deceptive Devices.

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5, 17 C.F.R. 240.10b-5. Employment of Manipulative and Deceptive Devices.

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of dealing which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

Petitioner is the wife of Bennie Taylor, formerly the largest shareholder of Southern Bancorporation. [JA 403 (7-10); 441 (13-15); 609 (9-11)]. Southern was a South Carolina bank holding company which owned all of the common stock of Southern Bank and Trust Company and World Acceptance Corporation. [JA 297 (13) - 298 (2)]. Mr. Taylor had founded World Acceptance. [JA 292 (19-21)]. In February, 1984 he was its Chief Executive Officer [JA 601 (6-7)] and a member of Southern's Board of Directors and Executive Committee. [JA 297 (7-14); 608 (3-8)]. Mr. and Mrs. Taylor together held 4.9 percent of Southern's stock. [JA 616 (13-17); 629 (18-22)].

In March of 1983 Mr. Taylor had an operation to ease pain derived from a previously amputated leg. [JA 560 (7-10)]. Complications from that operation left him a paraplegic [JA 402 (5-11)], confined him to a wheelchair, and caused him substantial discomfort. [JA 401 (18-19); 430 (23-25); 518 (5-7)]. He was also experiencing financial problems. [JA 506(5-8); 506(17) - 507(2)]. Southern was aware of Mr. Taylor's "precarious financial position." [JA 506(18), (21-22)].

On January 11, 1984, a meeting was held between high-level representatives of Southern and First Union Corporation. [EA 1-5]. This meeting was convened at the invitation of the Chief Executive Officer of First Union. [EA 1]. In attendance were the Board Chairman, President, Chief Financial Officer and legal counsel for First Union and the Chief Exec-

utive Officer, Vice Chairman, Vice President, Secretary and chief securities lawyer for Southern. [JA 275(25) - 276(26); 394 (19-20); 395 (12-22)]. At this meeting, First Union expressed an interest in acquiring the maximum amount of Southern stock they could at the time under Federal Reserve Regulations, which was 4.99 percent [JA 278(15-17); 622 (11-21)], approximately the same number of shares held by the Taylors. [JA 629 (18- 22)].

At that meeting First Union's Chief Executive Officer announced his company's interest in "developing a relationship similar to pinning as that term was used in the social context 30 years ago or so." [EA 1]. This pinning relationship was to look forward to First Union's eventual acquisition of Southern once approval of interstate banking occurred. [EA 5; JA 232 (2-11)]. According to the report of the meeting by Southern's SEC counsel, First Union's representatives announced its intention to buy Southern stock "on the basis of a gentleman's agreement of approval by Southern," [EA 1], and noted "that First Union has never owned any stock of any bank for take-over purposes *heretofore.*" *Id.* (Emphasis added.) First Union also raised the "likely possibility" that it would fund Southern's acquisition of other South Carolina banks, *id.*, thereby enhancing First Union's market penetration in South Carolina once interstate banking was permissible. Southern's lawyer's notes make clear that at the January 11, 1984 meeting, speaking on behalf of Southern, he informed First Union that, under the circumstances, "it appeared to us that disclosure was required." *Id.* That same lawyer's notes on the January 11 meeting refer both to a "contract to accomplish a merger when allowed by applicable law," *id.*, and to an agreement "in principle to merge when interstate banking was permissible." [EA 5; JA 232 (2-11)].

First Union's plan to acquire Southern's stock was blessed by Southern's Executive Committee, [JA 569 (12-16)]], and on February 2, 1984, First Union was notified that it could commence acquiring its nearly 5 percent stake in Southern stock, [EA 22; JA 630(9-16)]], a stake nearly identical to that held by petitioner and her husband.

Southern's Chief Executive Officer testified at trial that he had a "real strong motive to see this transaction take place," [JA 637(19) - 638(2)], that he knew petitioner and her husband held "approximately the same number of shares [First Union] wanted to buy," [JA 608(18-20)], and that petitioner's husband had previously stated that he would sell his stock if he ever ceased to be employed by World Acceptance, Southern's subsidiary [JA 609(12) - 610(1); 629(8-22)]. Four days after Southern gave First Union the go-ahead on the "pinning" relationship, petitioner's husband was fired at a meeting he was tricked into attending based on an intentionally falsified agenda. [JA 306 (3-9)]. As Southern had anticipated, petitioner's husband immediately indicated at the meeting his desire to sell his stock. [JA 296 (8-11); 607 (21-22); 616(12)]. Two days later he was notified by Southern that if he did not agree to sell his Southern stock by February 19, within two weeks, his salary and all of his disability benefits would be terminated. [EA 26].

A Goldman Sachs representative subsequently was able to get petitioner's husband to commit to a price of $18.00 per share for his stock. [JA 443 (1-2)]. The prospective buyer was represented by the Goldman Sachs agent to be "out on a yacht fishing." [JA 413(23) - 414(2)]. In reality, it was First Union. [JA 414 (13-15); 478(15-19)]. First Union's involvement was not disclosed until after petitioner's husband had committed himself on a price of $18.00 per share and taken a position on selling his block of stock, [JA 489 (1-9)], which included petitioner's stock as "part of the deal - part of the package." [JA 551(18) - 552(1)]. The cooperative behavior of Southern and First in divesting petitioner and her husband of their stock is evidenced by various facts in the record, including a provision in Mr. Taylor's agreement with Southern settling his employment claims requiring that he sell "all [Southern] stock owned directly and *indirectly* by him to First Union." [EA 64, 3]. Additionally, there was evidence that respondents conspired to keep one of Mr. Taylor's fellow board members from bidding for his stock. [EA 33, 42. JA 364(16) - 365(24); 271(20-25); 294(16) - 296(23); 589(4) - 590(3)].

After the purchase of petitioner's stock by First Union was consummated, Southern's press release continued the conspiracy of silence about the secret pinning and "gentleman's agreement" with First Union, stating: "It is important to make clear that there are no commitments or understandings between our companies." [EA 67].

Subsequently, fourteen days after interstate banking became permitted in South Carolina in 1986, Southern's shareholders approved a merger with First Union. [EA 101; 92, 1]. First Union acquired Southern by merger at $33.00 per share. [JA 811(17)]. No public disclosure of the banks' January 1984 "pinning" was ever made.

The theory of petitioner's complaint was that respondents had conspired to violate her rights as an investor in violation of Rule 10b-5 and in violation of South Carolina state law based on a conspiracy to violate a fiduciary duty owed to a minority shareholder. The jury was expressly instructed that nondisclosure under Rule 10b-5 only is actionable in the face of a duty to disclose which can be established due to a relationship of trust and confidence. [JA 804(22) - 805(4)]. The jury was also fully instructed on aider and abettor liability [JA 807(16)-(25)] and on civil conspiracy [JA 807(25) - 809(14)]. The jury was also instructed that only Southern could be directly liable on the fiduciary duty claim under state law. [JA 810(23) - 811(3)]. The jury was instructed that First Union's potential liability on the state law claim rested solely on petitioner's conspiracy allegations. [JA 811(4-11)]. The jury's findings for petitioner on both the 10b-5 and state law claim against both defendants thus shows the jury found a conspiracy between First Union and Southern to injure petitioner.

In reversing, the Fourth Circuit held that First Union and Southern's silence about their pinning relationship was neither misleading nor deceptive as a matter of law. Silence was actionable, held the court, only when silence would make other statements misleading or false. See pp. 5a-6a *infra*. Implicit in its ruling was the judgment that the identity of a buyer of stock is not a material fact that might be made

misleading by nondis- closure of such a circumstance as a pre-existing "pinning" relationship.

The Fourth Circuit also held there was no basis for a jury question on the issue of materiality. See pp. 6a-8a, *infra.* Totally absent from the circuit court's opinion is any reference to the notes written by Southern's SEC counsel, admitted into evidence, which reported his admonition at the January 11, 1984, meeting: "Speaking on behalf of Southern Bancorporation, I indicated that it appeared to us that disclosure was required." [EA 1].

The Fourth Circuit also held that any misrepresentations made by respondents were "in connection" with Mr. Taylor's firing, and "only tangentially and incidentally related to the sale of plaintiff's stock." See pp. 8a-11a, *infra.* Absent from the appellate court's opinion is any reference to the fact established at trial that Southern knew of Mr. Taylor's commitment that he would sell his Southern stock if he ceased to be employed by World. [JA 609(18) - 610(1); 629(10)-(17)].

REASONS FOR GRANTING THE WRIT

I.

The Fourth Circuit's restrictive reading of the "in connection with" requirement of Rule 10b-5 is at odds with the teaching of this Court and the law of other circuits.

This Court, in *Superintendent of Insurance v. Bankers Life and Casualty Co.*, 404 U.S. 6, 12 (1971), cautioned that "Section 10(b) must be read flexibly, not technically and restrictively." In *Rochelle v. Marine Midland Grace Trust Co.*, 535 F.2d 523 (9th Cir. 1976), the circuit court called attention to:

> [T]he roomy language of *Superintendent of Insurance v. Bankers Life and Casualty Co.* (1971) 404

> U.S. 6, 92 S.Ct. 165, 30 L.Ed2d 128. Although Section 10(b) was not meant to cover "internal mismanagement," "[t]he crux of the present case is that Manhattan suffered an injury as a result of deceptive practices touching its sale of securities as an investor." (*Id.* at 12-13, 92 S.Ct. at 169, 30 L.Ed.2d at 134). *Bankers Life* was undoubtedly intended to prevent courts from reading the phrase "in connection with" grudgingly.

Id at 529.

The Ninth Circuit's interpretation of the Supreme Court's intent in Bankers Life is mirrored by other decisions. *E.g.*, *Smallwood v. Pearl Brewing Co.*, 489 F2d 579, 595 (5th Cir. 1974) (observing the Court had made it clear that "a direct or close relation between the fraud and the securities transaction was not required" and noting that in *Bankers Life* the Court permitted a purchase by the plaintiff in one transaction to create standing to allege a 10b-5 violation in another transaction when both transactions were alleged to be part of the same scheme); *Halperin v. Jasper*, 1987 WL 20192 (E.D. Pa. 1987) (equating the "in connection with" requirement with a "but for" test); *First Federal Sav. and Loan Ass'n v. Oppenheim, Appel, Dixon & Co.*, 629 F. Supp. 427, 440 (S.D.N.Y. 1986) (referring to the "broad 'touch' test enunciated in *Superintendent.*"). A leading treatise on § 10(b) and Rule 10b-5 suggests that the "connection" between fraud and a securities transaction "can be very tenuous," 2 Bromberg & Lowenfels, *Securities Fraud & Commodities Fraud* § 4.7(574)(3), at 88.34 (1982). *See also* Note, The Pendulum Swings Farther: The "In Connection With" Requirement and Pretrial Dismissals of Rule 10b-5 Private Claims for Damages, 56 *Tex. L. Rev.* 62 (1977).

In holding that the "in connection" test had not been satisfied, Judge Wilkinson, writing for the Fourth Circuit panel, relied on two cases. The first was on his own recent ruling in *Hunt v. Robinson*, 852 F.2d 786, 787-88 (4th Cir. 1988), wherein he postulated that the "goal [of section 10(b)]

is not furthered by bringing within the ambit of § 10(b) claims amounting to . . . common law fraud which have long been the staple[] of state law." This political statement collides directly with the entire recent thrust of Supreme Court decisions interpreting Rule 10b- 5 to require proof of fraud in the classic common law sense. *E.g., Chiarella v. United States*, 445 U.S. 222, 234-35 (1980) (observing that "[s]ection 10(b) is aptly described as a catchall provision but what it catches must be fraud."). In any event, *Hunt* is distinguishable because the wrong there was purely in refusing to issue stock under the terms of a contract. There was no clear evidence in *Hunt* that, as here, the making of the stock sale contract itself was tainted by fraud. To claim, as did the Fourth Circuit, "that the controversy here related primarily to the unpleasant circumstances surrounding Bennie Taylor's termination," ignores the evidence in the record that termination and stock sale were intertwined due to Mr. Taylor's commitment to sell the stock if he left World Acceptance. It also ignores the proof that Southern itself admitted, through its securities counsel, that disclosure was required for the protection of investors.

The only other case relied on by Judge Wilkinson, *Tully v. Mott Supermarkets, Inc.*, 540 F.2d 187, 194 (3d Cir. 1976), simply required that "there be some causal connection between the alleged fraud and the purchase or sale of stock." *Id.* It has been questioned whether *Tully's* "causal connection" requirement is the same as 10b-5's "in connection with" requirement. *Ketchum v. Green*, 557 F.2d 1022, 1028 (3d Cir. 1977). In any event, even if a "but for" test is required, it is satisfied on the present facts, for petitioner and her husband were victims of deception as to his dismissal and also as to the crucial relation between First Union and Southern at the time of the stock sale.

II.

Conspiracies to defraud are actionable under Rule 10b-5 and petitioner proved one.

Rule 10b-5 makes it "unlawful for any person, directly or *indirectly*" to engage in the prohibited conduct. 17 C.F.R. 240.10b-5. Numerous lower courts have upheld claims premised on conspiracies to violate rule 10b-5. *See, e.g., SEC v. Seaboard Corp.*, 677 F.2d 1297, 1299 (9th Cir. 1982):

> Fringe participants in illegal securities transactions have been brought within the scope of the securities laws with the application of criminal and tort theories of liability. Alleged coconspirators have been held liable for the acts of direct violators of § 10(b) and Rule 10b-5, when they knew of the fraud and assisted the overall scheme. *See, e.g., Dasho v. Susquehanna Corp.*, 380 F.2d 262 (7th Cir.), cert. denied, 389 U.S. 977, 88 S.Ct. 480, 19 L.Ed.2d 470 (1967); *Texas Continental Life Ins. Co. v. Dunne*, 307 F.2d 242 (6th Cir. 1962); *Kardon v. National Gypsum Co.*, 69 F.Supp. 512 (E.D.Pa.1946).

See also Rose v. Arkansas Valley Environmental & Utility Authority, 562 F.Supp. 1180, 1211-12 (W.D. Mo. 1983). In *Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 394 (1982), this Court held that those who conspire to violate the Commodities Exchange Act can be held accountable under the act. However, the Court in *Hochfelder v. Ernst & Ernst*, 425 U.S. 185, 191-92 n.7 (1976), expressly reserved the question whether indirect liability under Rule 10b-5 could be imposed on aiders and abettors, and this Court has never held that 10b-5 reaches coconspirators.

The jury in this case was instructed on conspiracy and unquestionably found a conspiracy to defraud. The appellate court expressed its disdain for conspiracy theory by suggesting that "[f]ederal securities law was not intended to ... substitute for the more general state claims of ... conspiracy

[or] fraud. . . ." See pp. 10a-11a, *infra.* The court then proceeded to proclaim that "[w]here companies have complied with the requirements of § 10(b), we decline to interpret state corporate law to find a conspiracy. . . ." See pp. 11a-12a, *infra.* The unfair *Catch-22* problem for petitioner is obvious.

The record is strewn with facts supporting petitioner's conspiracy theory. Both the trial judge and respondents' counsel well understood they were trying a conspiracy case.[1] Apart from the highly incriminating notes of Southern's SEC counsel, which were never mentioned by the appellate court, there was ample evidence of a conspiracy presented at trial. Southern's Press Release issued upon First Union's purchase of the Taylors' stock declared, falsely: "[I]t is important to make it clear that there are no commitments or understandings between our companies." [EA 67].[2] However, notes written by a First Union Senior Vice President are to the contrary [JA 68-83]. The First Union executive who negotiated the Taylor stock purchase refers to an "agreement in principle" [EA 74], an "agreement to merge," [EA 73], and to the conspiracy of silence: "Basic strategy—low key the transaction as a 'non event.' "[EA 72]. First Union's take-over of Southern was approved within two weeks after interstate banking became effective in South Carolina. [EA 92]. This is additional evidence that there was, in fact, an agreement in principle to merge as soon as interstate banking was permitted.

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[1] MR. CALHOUN: Your Honor, may I be heard because this is exceedingly important to—
THE COURT: I'll listen to you, but—
MR. CALHOUN: Sir?
THE COURT: I'll listen to you, but you're trying a conspiracy case.
MR. CALHOUN: Yes sir.

[2] If, as the Fourth Circuit held, the existence of the pinning relationship agreement was not a material fact, then why did Southern attempt in its release to deny (falsely) the existence of such an agreement? Clearly, Southern thought news of the existence of an understanding between it and First Union would be important to investors.

Additional evidence of conspiracy is found in the legal opinion of Southern's counsel dated February 28, 1984, [EA 55-60]. It states that it is based on "information that [Southern] have furnished us." [EA 56]. It further states that Mr. Taylor was fired based on "substantial disputes" which arose "[i]n early February 1984" [EA 58]. Mr. Taylor was fired on Monday, February 6, 1984 [EA 26]. This means that the "substantial disputes" had to have arisen over the first few days of February, but there is no evidence whatever in the record of any such disputes during that period. The Taylor firing occurred shortly after the January 11 meeting at which First Union sought to acquire 4.9 percent of Southern's stock, *exactly* what the Taylors held. Southern knew Taylor would sell his stocks if he was terminated [JA 609(14) - 610(1); 629 (8-22)] and lied to him to induce him to attend the meeting at which he was fired [JA 306(3- 9)]. The Fourth Circuit admitted petitioner had proved an "agreement" between First Union and Southern prior to her sale. See p. 7a, *infra*. Previously this was denied by Southern in the press release it put out immediately after petitioner's sale to First Union, admonishing that, "It is *important* to make clear that there are no commitments or understandings between our companies." [EA 67]. (Emphasis added.)

The foregoing evidence was in the record and the jury was instructed on conspiracy. There was ample evidence to support liability based on either a conspiracy to violate the federal securities laws or to breach fiduciary duties owed under state law.[3] Absent from the appellate court's opinion is

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[3] The appellate court's ruling that there was not a fiduciary bond between petitioner and Southern, see p. 12a, *infra*, was clearly wrong. South Carolina's courts have traditionally viewed the concept of a fiduciary relationship, or a relationship of trust and confidence, very flexibly. They have been "careful to not define fiduciary relationships so as to exclude new cases that may give rise to the relationship." *Island Car Wash, Inc. v. Norris*, 292 S.C. 595, 599, 358 S.E.2d 150, 152 (Ct. App. 1987). South Carolina's Court of Appeals has held that a fiduciary relationship could arise between a bank and one of its customers. *Rush v. South Carolina*

any justification for its reversal of the jury's conspiracy liability determination.

III.

The Fourth Circuit's decision is irreconcilable with *Levinson v. Basic, Inc.*, 108 S.Ct. 978 (1988).

In *Basic* this Court held that a "fact specific" inquiry was called for in order to determine when merger discussions became so material as to require disclosure. *Levinson v. Basic, Inc.*, 108 S.Ct. 978, 988 (1988). The Court called attention to the need "to look to indicia of interest in the transaction at the highest corporate levels." *Id.* at 987. In particular, the court noted factors such as "board resolutions, instructions to investment bankers and actual negotiations between principals" as serving as indicia of interest. *Id.* Here, the

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National Bank, 288 S. C. 560, 343 S.E.2d 667 (Ct. App. 1986). *See also Steele v. Victory Savings Bank*, 295 S.C. 290, 368 S. E.2d 91 (Ct. App. 1988). If a bank can owe a fiduciary duty to a *customer*, it can naturally be viewed as in a fiduciary relationship with one of its own *shareholders*, as the lower court held. See pp. 17a-18a, *infra*. This is particularly so in South Carolina, given that shareholders are *express, direct* beneficiaries of a statutory duty of good faith owed by the directors of South Carolina corporations, such as Southern. *See* South Carolina Code § 33-13-150 (1987). No other state has such a statutory provision. Petitioner was not just a Southern shareholder, however. Her husband was a Southern fiduciary. The Fourth Circuit's ruling on the fiduciary duty issue is clear error in applying South Carolina law. Moreover, even if a fiduciary duty was absent, the civil conspiracy was *per se* actionable under controlling South Carolina authority. *See LaMotte v. Punch Line*, 296 S.C. 66, 370 S.E.2d 711 (1988) (actionable civil conspiracy may exist even though all elements of another wrong are not present). A reasonable way to rectify the error is for this Court to follow the procedure it used in *Lehman Brothers v. Schein*, 416 U.S. 368, 94 S.Ct. 1741, 40 L.Ed.2d 215 (1974), and remand the case to the Fourth Circuit with a suggestion that it consider use of South Carolina Supreme Court Rule 46, the Rule for Certification of Questions of Law. That rule is available for use by "any federal court of the United States." *Id.*

record reflects that, immediately prior to petitioner's stock sale, there was approval of the "gentleman's agreement" by Southern's Executive Committee, participation by investment banker Goldman Sachs on behalf of First Union in obtaining the sought-after 4.9 percent stake in Southern from petitioner and her husband, and actual negotiations between the principals. Not just was every base mentioned in *Basic* touched, but Southern's securities counsel, speaking on behalf of Southern, announced to First Union that, under the circumstances, "it appeared to us that disclosure was required." All the jury did was agree with Southern. Clearly a material fact, the "gentleman's agreement," was withheld from petitioner, and disclosure of that material fact was needed to make the fact that was known, the buyer's identity, not misleading.

Perhaps most telling on the materiality issue is the fact that Southern's press release, issued immediately following petitioners' sale, stated it was "*important* to make clear there are no understandings between our companies." [EA 67] (Emphasis added.) The press release was never mentioned by the Fourth Circuit. The release raises a good question, however, in light of the Fourth Circuit's finding of an agreement between First Union and Southern. The question is, if the *absence* of an agreement is an "important" (*i.e.*, material) fact, as the Southern press release stated, then how can the *existence* of an agreement be immaterial as a matter of law? The appellate court's application of *Basic* is clearly wrong and ill-serves the investing public.

Missing from the appellate court's analysis is any recognition that this case presents classic insider trading, invoking the disclose-or-abstain rule that has been unchallenged since the landmark case of *SEC v. Texas Gulf Sulphur*, 401 F.2d 833 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969).

CONCLUSION

For these various reasons, this petition for certiorari should be granted.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

Patricia B. TAYLOR, Plaintiff-Appellee,
versus
FIRST UNION CORPORATION OF SOUTH CAROLINA, formerly Southern Bancorporation, Inc.; First Union Corporation, Defendants-Appellants.

No. 88-2503.

Appeal from the United States District Court for the District of South Carolina, at Greenville. G. Ross Anderson, Jr., District Judge. (CA-87-459).

Argued June 9, 1988.
Decided Sept. 22, 1988.

Before RUSSELL and WILKINSON, Circuit Judges, and NIEMEYER, United States District Judge for the District of Maryland, sitting by designation.

John Thompson Allred, Charlotte, N.C. (Kenneth S. Broun, J. Anthony Penry, Petree, Stockton & Robinson, Winston-Salem, N.C., O.G. Calhoun, William M. Grant, Jr., Haynsworth, Marion, McKay & Guerard, Greenville, S.C., Francis C. Clark, Legal Div., First Union Corp., Winston-Salem, N.C., on brief), for defendants-appellants. John Patrick Freeman, Columbia, S.C., J. Kendall Few, Greenville, S.C., for plaintiff-appellee.

WILKINSON, Circuit Judge:

In February 1984, plaintiff Patricia Taylor and her husband, Bennie Taylor, sold their stock in Southern Bancorporation, Inc. to First Union Corporation for $18 a share. In September 1985, Southern and First Union entered into a merger agreement, and First Union offered to purchase all outstanding stock in Southern for $33 a share. Plaintiff filed suit against Southern and First Union alleging violations of § 10(b) of the Securities Exchange Act of 1934 and breach of fiduciary duty in connection with defendants' failure to disclose their merger discussions and their conduct surrounding the purchase of her stock. A jury returned a verdict in favor of plaintiff on both the state and federal claims and awarded her damages based on the difference between her selling price and the later acquisition price of the Southern stock.

Because § 10(b) imposed no obligation on defendants to disclose highly tentative merger discussions prior to plaintiff's sale of her stock and because defendants' conduct did not constitute deception in connection with the sale of stock or a breach of any fiduciary duty owed to plaintiff, we reverse and remand for entry of judgment in favor of defendants.

I.

Southern Bancorporation (Southern) was a South Carolina bank holding company that owned all of the common stock of Southern Bank & Trust Co. and World Acceptance Corp. Plaintiff, Patricia Taylor, and her husband, Bennie Taylor, owned 4.9% of the stock in Southern. In February 1984, Bennie Taylor was the Chief Executive Officer of World Acceptance and a member of the board of directors and executive committee of Southern. Bennie Taylor underwent surgery in March of 1983 which left him a paraplegic and resulted in serious emotional complications.

On January 11, 1984, representatives of First Union, a North Carolina bank holding company, met with representatives of Southern to discuss the possibility of the two companies developing a "relationship." Bennie Taylor was

not present at this meeting. The evidence indicates that First Union raised the possibility of a merger with Southern in the event interstate banking became legal. First Union also expressed an interest in acquiring 4.99% of Southern's stock. Southern's board of directors met on January 31, 1984. Bennie Taylor was present at that meeting. After the board meeting, Southern's executive committee approved First Union's acquisition of Southern's stock. First Union then began acquiring stock on the market at the prevailing market price of $16 per share.

On February 6, 1984, a special executive committee of Southern's board sought Bennie Taylor's resignation, allegedly because his deteriorating physical and mental condition made him unable to fulfill his responsibilities to the company, prompting the resignation of three senior officers and executives of World Acceptance. When Bennie Taylor refused to resign, he was terminated. Taylor apparently indicated at that time that he intended to sell his stock in Southern, and he subsequently retained an attorney to negotiate a sale. On February 8, 1984, Southern sent a letter to Taylor offering to pay his salary and benefits through December 31, 1984 if Taylor would agree to resign all offices and directorships at Southern and World Acceptance, to sell his stock in Southern to the company for fair market value, and to release Southern and World Acceptance from all claims arising from his employment and termination. The letter indicated that if Taylor did not accept the offer by February 19, 1984, his salary and all benefits would terminate on February 29, 1984.

Bennie Taylor subsequently offered to sell his stock to Southern for $18 per share, approximately $2 per share above market value. Southern declined to purchase the stock at that price and Taylor's attorney subsequently negotiated a sale of the stock to First Union for $18 per share. On February 28, 1984, Bennie Taylor executed a settlement memorandum prepared by Southern stating that he would sell all stock in Southern owned directly or indirectly by him to First Union for $18 per share. This agreement anticipated as well the sale

of the stock owned by plaintiff, Patricia Taylor. Plaintiff was persuaded by Bennie Taylor and his attorney to sell her stock to First Union.

In June 1985, the Supreme Court, in *Northeast Bancorp, Inc. v. Board of Governors of the Federal Reserve System*, 472 U.S. 159, 105 S.Ct. 2545, 86 L.Ed.2d 112 (1985), held that interstate banking was constitutional. Subsequent state enabling legislation authorized the merger of North Carolina and South Carolina banks as of January 1, 1986. On September 15, 1985, Southern's president met with representatives of First Union to discuss a proposed merger. An agreement was negotiated authorizing First Union to purchase all of Southern's common stock for $33 per share. Southern's executive committee recommended acceptance of First Union's offer on September 20, 1985. The boards of Southern and First Union subsequently approved the merger and the merger took place, effective April 1, 1986.

Patricia Taylor filed suit in the United States District Court for the District of South Carolina. Her husband, Bennie Taylor, subsequently filed a companion suit on an apparently similar theory. Bennie Taylor's suit has been stayed pending the outcome of this appeal. Patricia Taylor's complaint alleged that Southern and First Union had conspired to withhold from her and her husband information concerning the proposed merger between the two companies in order to acquire their stock at less than its true value. This, plaintiff claims, violated § 10(b) of the Securities Exchange Act and breached the fiduciary duty owed to her by defendants. The action resulted in a mistrial on October 12, 1987, and was retried before a jury on November 16, 1987. The jury returned a verdict against both defendants on both claims in the amount of $165,975 plus interest and costs. Defendants' motion for judgment n.o.v. or for a new trial was denied and defendants appeal.

II.

Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder makes it unlawful for any person

> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. 240.10b-5; *see* 15 U.S.C. § 78j(b).

We hold, as a matter of law, that plaintiff's allegations failed to state a claim under any prong of Rule 10b-5.

A.

Plaintiff contends that First Union and Southern violated Rule 10b-5 by failing to disclose that, at their January 11, 1984 meeting, they agreed to establish a relationship, described as similar to "pinning" as that term was used socially thirty years ago, and agreed in principle to merge when interstate banking became permissible. We disagree. To be actionable under Rule 10b-5(b), a statement or omission must be both material and misleading. *See Basic, Inc. v. Levinson*, ____ U.S. ____, 108 S.Ct. 978, 986-88, 99 L.Ed.2d 194 (1988); *Parsons v. Hornblower & Weeks-Hemphill, Noyes*, 447 F.Supp. 482, 489-90 (M.D.N.C.1977), *aff'd*, 571 F.2d 203 (4th Cir.1978). Because their silence was neither material nor misleading, First Union and Southern were under no obligation to disclose to the Taylors their January 11, 1984 discussions of the possibility of a future merger.

The Supreme Court has recognized that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5." *Basic*, 108 S.Ct. at 987 n. 17; *see Jordan v. Duff & Phelps, Inc.*,

815 F.2d 429, 431 (7th Cir. 1987) ("a law designed to prevent frauds on investors tolerates silence that yields benefits for investors as a group"). Rule 10b-5 imposes such a duty to disclose only when silence would make other statements misleading or false. *Parsons*, 447 F.Supp. at 490; *Wessel v. Buhler*, 437 F.2d 279, 283 (9th Cir.1971). Plaintiff has failed to identify any statement made misleading by the defendants' nondisclosure of their merger discussions. There is no allegation that defendants had previously denied the possibility of a merger at some future time. In fact, in its 1980 annual report, Southern was identified as a potential acquisition target should interstate banking become legal.

In addition to not being deceptive, the omission complained of here was not material. In the proxy solicitation context, "[a]n omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449, 96 S.Ct. 2126, 2132, 48 L.Ed.2d 757 (1976); *Basic*, 108 S.Ct. at 983. The materiality of merger discussions depends on the surrounding facts and circumstances. *Basic*, 108 S.Ct. at 987-88. Merger negotiations in *Basic* had progressed to a stage well beyond that presented here and the prospect of a merger there was far more concrete. The Federal Trade Commission had removed regulatory barriers to Basic's merger with Combustion Engineering in 1976. During the next two years Basic and Combustion engaged in meetings, discussions, and negotiations concerning a future merger. *Id.* at 981. The Sixth Circuit noted that attorneys had prepared analyses and evaluations for use in the merger negotiations and investment bankers had been engaged to facilitate the merger. *Levinson v. Basic, Inc.*, 786 F.2d 741, 743-45 (6th Cir.1986), *vacated and remanded*, ____ U.S. ____, 108 S.Ct. 978, 99 L.Ed.2d 194 (1988). In that time, in response to heavy trading in its stock, Basic issued three public denials of any knowledge of merger discussions. *Basic*, 108 S.Ct. at 981. Even on these facts, the Supreme Court refused to hold that disclosure was required and instead remanded the case for reconsideration of the

materiality question. *Id.* at 988.

In contrast to the circumstances of *Basic*, the evidence indicates that the discussions at issue here were preliminary, contingent, and speculative. At best, the merger discussions culminated in a vague "agreement" to establish a relationship. There was no agreement as to the price or structure of the deal. While, after *Basic*, this alone is not dispositive of the question of materiality, it is certainly not irrelevant to the totality of the circumstances test articulated in that case. Furthermore, neither the factual nor the legal predicates for a merger were in place. There is no evidence of board resolutions, actual negotiations, or instructions to investment bankers to facilitate a merger. *See Basic*, 108 S.Ct. at 987. A merger between First Union and Southern was contingent on events beyond the control of the parties. At the time First Union purchased plaintiff's stock, the Supreme Court had yet to rule on the constitutionality of interstate banking, and no merger could take place until enabling legislation was enacted both in North Carolina and South Carolina. The evidence also suggests that First Union sought unsuccessfully to acquire either of two other South Carolina banks, South Carolina National Bank and C & S of South Carolina, before merging with Southern.

In sum, any "pinning" relationship between First Union and Southern at the time of the purchase of plaintiff's stock was of a fickle and changeable character. Those in business routinely discuss and exchange information on matters which may or may not eventuate in some future agreement. Not every such business conversation gives rise to legal obligations. We recognize, of course, the unique significance of a merger in the life of a corporation and do not hold that the high mortality rate of proposed mergers absolves management of all duty to disclose. *See Basic*, 108 S.Ct. at 987; *SEC v. Geon Industries, Inc.*, 531 F.2d 39, 47-48 (2d Cir.1976). The element of materiality, required by the express terms of Rule 10b-5, serves, however, to define the limits of disclosure under federal securities law. *See TSC Industries*, 426 U.S. at 448-49, 96 S.Ct. at 2131-32. The materiality of information

concerning a proposed merger is directly related to the likelihood the merger will be accomplished; the more tentative the discussions the less useful such information will be to a reasonable investor in reaching a decision. Information of speculative and tentative discussions is of dubious and marginal significance to that decision. To hold otherwise would result in endless and bewildering guesses as to the need for disclosure, operate as a deterrent to the legitimate conduct of corporate operations, and threaten to "bury the shareholders in an avalanche of trivial information"; the very perils that the limit on disclosure imposed by the materiality requirement serves to avoid. *See id.; Susquehanna Corp. v. Pan American Sulphur Co.*, 423 F.2d 1075, 1085-86 (5th Cir.1970).

B.

Plaintiff's claim that First Union and Southern violated Rule 10b-5 by employing a "device, scheme, or artifice to defraud," and by engaging in an "act, practice, or course of business which operate[d] . . . as a fraud or deceit upon any person" is likewise without merit.

Claims for violations of § 10(b) that do not involve a material misrepresentation or nondisclosure must include some element of deception. *See Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 473-77, 97 S.Ct. 1292, 1300-03, 51 L.Ed.2d 480 (1977). The district court concluded that there was "sufficient evidence of deception by Defendants to satisfy this rule." In addition to the nondisclosure of the "pinning agreement," the district court pointed to evidence indicating that Southern lied to plaintiff's husband about the purpose of the meeting at which the company sought his resignation, that Southern threatened to terminate Bennie Taylor's benefits unless he agreed to sell his stock, that First Union's broker misrepresented the identity of his principal until Bennie Taylor committed to a sales price of $18 per share, and that Southern knew but did not disclose that a member of its board had expressed an interest in purchasing the Taylors' stock.

The district court, however, did not address the additional requirement of Rule 10b-5, that the scheme, artifice, fraud, or deceit complained of must occur "in connection with the purchase or sale of [a] security." Defendants' conduct, however characterized, cannot fairly be said to have been "in connection with" the stock sale. *Hunt v. Robinson*, 852 F.2d 786, 787 (4th Cir.1988); *Tully v. Mott Supermarkets, Inc.*, 540 F.2d 187, 194 (3rd Cir.1976).

An examination of the separate points relied upon by the district court supports the conclusion that the controversy here related primarily to the unpleasant circumstances surrounding Bennie Taylor's termination rather than to any claim cognizable under the federal securities laws. The alleged acts of deception here most directly involve the circumstances of that termination and are only tangentially and incidentally related to the sale of plaintiff's stock.

Taking the inferences, as we must, in favor of the prevailing party below, any misrepresentations concerning the purpose of the meeting at which Taylor was terminated were plainly not in connection with the stock sale, but rather, in connection with the discharge. As for Southern's alleged failure to disclose that a member of its board had expressed an interest in purchasing the Taylors' stock, we note that § 10b-5 [sic] imposes on a prospective purchaser no obligation to disclose to a seller the identity of every other potentially interested party. The so called "threat" to terminate Taylor's benefits, involved nothing more than negotiations over the terms and conditions of his departure and involved no *fraud* in connection with the sale of a security. Southern's letter to Taylor, rather than relating to disability benefits which all concede were vested, spoke in addition to benefits generally in terms of salary, perquisites, office space, secretarial assistance, and matters which would have to be addressed in any discussion of the terms of a departure. There is, in fact, little to distinguish it from customary negotiations over an officer's or director's severance arrangements. Finally, any misrepresentation by the broker of the identity of his principal is insufficient to transform the character of this entire

controversy into one of fraud under § 10(b). There was no misrepresentation of the value of the stock. While Bennie Taylor claims that he was too far committed to the deal at the time, he did learn prior to any consummation of the sale that First Union was the purchaser. Moreover, the broker apparently misinformed Taylor that he could not accept the offer because "his principal was out on a yacht fishing" only after Taylor, over his attorney's advice not to commit, quoted a price of $18 per share. The plaintiff was not misled in her investment decision by the nondisclosure of material information nor was she deceived about the value of the stock or the potential value of the company. Thus, the requisite nexus between the sale and any fraud or deception is simply lacking.

While not dispositive of plaintiff's claim under § 10(b), it is, nonetheless, significant that Bennie Taylor was a sophisticated investor and a member of the board of directors of Southern. Bennie Taylor was not unknowledgeable about the company and the banking industry and was aware of the implications of interstate banking for the company. The evidence indicates that he attended the director's meeting at which First Union's investment in Southern was approved. He knew that Southern presented an attractive acquisition target should interstate banking become legal. *See, e.g., Seibert v. Sperry Rand Corp.*, 586 F.2d 949, 952 (2d Cir.1978). Although he was in poor health, Bennie Taylor negotiated the stock sale through an attorney who testified that he advised caution in the sale and informed Taylor of the possibility of a First Union-Southern merger.

The fundamental purpose of the Securities Exchange Act is to implement a "philosophy of full disclosure," *Santa Fe Industries*, 430 U.S. at 477-78, 97 S.Ct. at 1302-03, by ensuring that the reasonable investor receives the information necessary to make informed investment decisions. *See Hunt*, 852 F.2d at 787; *O'Brien v. Continental Illinois Nat. Bank & Trust*, 593 F.2d 54, 60 (7th Cir.1979). Federal securities law was not intended to provide a federal forum for every intracorporate squabble or to substitute for the more general state claims of wrongful discharge, conspiracy,

fraud, or duress which may, of course, be litigated in state court. The securities law does not authorize and its goals are not furthered by the scrutiny of the background of every factional struggle among directors or shareholders simply because the sale of stock happens to have taken place. This action is brought by Patricia Taylor in her capacity as a shareholder of Southern, and whatever state law actions Bennie Taylor may seek to bring for wrongful discharge or breach of fiduciary duty in his capacity as director are, of course, not before us.

III.

The evidence does not support the conclusion that, under South Carolina law, defendants breached any fiduciary duty owed to plaintiff, as a stockholder in Southern.

Under South Carolina law, "officers and directors of a corporation stand in a fiduciary relationship to the individual stockholders and in every instance must make a full disclosure of all relevant facts when purchasing shares of stock from a stockholder." *Jacobson v. Yaschik*, 249 S.C. 577, 155 S.E.2d 601, 605 (1967). The fiduciary obligation established by South Carolina law is quite specific. This fiduciary duty runs from the officers and directors of a corporation to the shareholders of their corporation. This relationship requires full disclosure of all material information when the officer or director seeks to acquire the company's stock from a shareholder. *See id.* 155 S.E.2d at 605-06; *Black v. Simpson*, 94 S.C. 312, 77 S.E. 1023, 1025 (1913); *see also* S.C. Code Ann. § 33-13-150 (1976). As such, the extent of the fiduciary obligation is both settled and predictable, and not subject to speculative expansion whenever some third party is involved.

Here, we do not address the case of a corporate officer or director (or even the corporation itself) purchasing the stock of one of its own shareholders. Rather we have one corporation, First Union, purchasing the stock of a second corporation, Southern, from a shareholder of that corporation. Where companies have complied with the requirements of

§ 10(b), we decline to interpret state corporate law to find a conspiracy in every business interaction. Similarly, we decline to extend South Carolina law to impose a fiduciary obligation on a corporation with respect to the purchase of its shareholder's stock by a second corporation, or on a corporation purchasing stock from the shareholder of another corporation, simply because the two corporations have had some prior business dealings or negotiations.

IV.

The securities markets are not meant to be risk-free. Patricia Taylor sold her stock in 1984 for $18 a share, $2 a share above its fair market value. She now seeks, and the jury has awarded her, damages in excess of $165,000, the difference between the price she received from First Union and the enhanced value of the securities two years hence.

A verdict based on these facts undermines the proper operation of the securities markets. Sales of securities remain market transactions. The seller receives cash for the stock, thereby ridding herself of the risk of a decrease in its value and simultaneously assuming the risk that its value might increase. The vital congressional purpose in protecting investors against uninformed decision-making is not intended to simultaneously eliminate all risk that the stock may increase by providing a cause of action against the corporation in that eventuality. Neither federal securities law nor the South Carolina law of fiduciary duty provides a remedy for a shareholder who, in hindsight, simply wishes that she had held onto her stock.

The judgment of the district court is

REVERSED.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
GREENVILLE DIVISION

Patricia B. Taylor,
Plaintiff,

vs.

First Union Corporation of South Carolina (formerly Southern Bancorporation, Inc.) and First Union Corporation,
Defendants.

C/A #: 6:87-459-3

ORDER

This is an action for violation of SEC Rule 10b-5 and for breach of fiduciary duty. The jury found for the Plaintiff and the Defendants moved for judgment notwithstanding the verdict and in the alternative for a new trial. For the reasons set forth below, the motion is denied.

Plaintiff claims that she and her husband were forced to sell their stock in Southern Bancorporation to First Union as a result of a series of events involving conspiracy, coercion and fraud. She alleged that the Defendants met secretly in January, 1984, and agreed in principle to merge as soon as interstate banking was permitted. She further alleged that the existence of this meeting and agreement were concealed from herself and her husband even though her husband was a member of the Executive Committee and Board of Directors of Southern Bancorporation. She further alleged that her husband was precipitously terminated by Southern Bancorporation and threatened with a termination of his disability benefits unless she and he agreed to sell all of their stock to First Union at $18.00 per share. She further alleged that the fact that another member of the Board of Directors desired to purchase their stock was concealed from them.

THE ROYALTY NOTES

As a part of her case, Plaintiff introduced a series of typed and handwritten notes from Southern Bancorporation's SEC compliance attorney. These notes were produced by the Defendants and authenticated by the deposition testimony of the author introduced by the Plaintiff at trial. Plantiff's Exhibit #1 consisted of the attorney's typed and handwritten notes of the allegedly secret January, 1984, meeting between the Defendants. Plaintiff's Exhibit #8 consisted of the attorney's handwritten notes of a series of interstate telephone calls to the Defendants concerning the termination of Plaintiff's husband and the acquisition of their stock by First Union.

Among other things, Plaintiff's Exhibit #1 contained evidence that the Defendants had discussed "possible investment alternatives" at the January, 1984, meeting, including to "agree in principle to merge when interstate banking is permissible." [Exhibit #1, p. 5]. These notes further indicate that during this meeting, the Chief Executive Officer of First Union "said that First Union had an interest in developing a relationship [with Southern Bancorporation] similar to 'pinning' as that term was used in social context 30 years or so ago." [Exhibit #1, p. 1]. Following what was referred to as a "gentlemen's agreement of approval by Southern Bancorporation," these notes show that Southern Bancorporation, speaking through its attorney, "indicated that it appeared to us that disclosure was required." [Exhibit #1, p. 2].

Exhibit #8 consisted of the attorney's notes of a series of interstate telephone calls between the attorney and others, including the Chairman of the Board and other officers of Southern Bancorporation and the inside General Counsel and other officers of First Union. Among other things, these notes show that sometime after February 14, 1984, the attorney "learned that Southern Bancorporation would prefer to buy Taylor's stock as opposed to *having First Union buy it.*" [Exhibit #8, p. 2, emphasis added]. Other notes indicate that Southern Bancorporation wanted to buy the Taylors' stock and to "keep First Union in the market." [Exhibit #8, p.

4]. They show knowledge on the part of Southern Bancorporation of a fellow board member's undisclosed desire to purchase the Taylor stock [Exhibit #8, pp. 7 and 16]. And they further show that on February 24, 1984, the Southern Bancorporation SEC compliance attorney telephoned the inside General Counsel for First Union to "encourage them to pursue [Plaintiff's husband] on their own." [Exhibit #8, p. 22].

These two exhibits were properly authenticated by the deposition testimony of their author and they both contain evidence that is clearly relevant to the issues of compliance with Rule 10b-5, breach of fiduciary duty and conspiracy. However, Defendants contend that they should have been excluded under the Hearsay Rule.

It is clear that these two exhibits contain statements admissible under Federal Rule of Evidence 801(d)2 both as admissions by the agent of a party opponent under 801(d)2(D) or as statements of a co-conspirator under 801(d)2(E).[1] Statements contained in these two exhibits also may be admissible under Federal Rules of Evidence 803(1) as a present sense impression,[2] under Rule 803(3) as statements

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[1] *See, generally,* 28 *U.S.C.S.* (Lawyer's Edition) Rule 801, notes 10.12, 16 and 18. For admissions by a co-conspirator, *see, U. S. v. Panza,* 750 F.2d 1141 (2d Cir. 1984); *U. S. v. Broome,* 732 F.2d 363 (4th Cir. 1984); *U. S. v. Kiefer,* 694 F.2d 1109, 1112-13 (8th Cir. 1982); and *U. S. v. Gibson,* 690 F.2d 697 (9th Cir. 1982). *See, also,* Annotation: 44 A.L.R. Fed. 627 (1979). For admissions both as agent and co-conspirator, *see, U. S. v. Ramsey,* 785 F.2d 184, 191 (7th Cir. 1986). For admissions by an agent, *see, Rule v. International Association,* 568 F.2d 558 (8th Cir. 1978); *Pino v. Protection Maritime Ins. Co.,* 599 F.2d 10 (1st Cir. 1979), *certiorari denied,* 444 U.S. 900, 100 S.Ct. 210, 62 L.Ed.2d 136 [statement by a broker]; *Nekolny v. Painter,* 653 F.2d 1164 (8th Cir. 1981); *Marshane Corp. v. St. Paul Fire & Machine,* 10 Fed. Evid. Rep. 1232 (4th Cir. 1982) [statements by an insurance claims representative]; *Materials Research Corp. v. BOC Group, Inc.,* 19 Fed. Rule Serv. 1167, 4 F.R.Serv.3d 85 (D.N.J. 1986) [statements by a consultant]; and *U. S. v. Young,* 736 F.2d 565 (10th Cir. 1983), reserved on other grounds, 470 U.S. 1, 105 S.Ct. 1038 (1985) [statements by an accountant].

[2] *See,* Annotation: 60 A.L.R. Fed. 524 (1982); *U. S. v. Margiotta,* 688 F.2d 108 (2nd Cir. 1982); *Brown v. Tard,* 552 F.Supp. 1341 (D.N.J. 1982); and *Coremaster v. U.S.,* 584 F.Supp. 1406 (N.D.Cal. 1984).

of the declarant's existing state of mind concerning intent, plan, motive and design,[3] under Rule 803(5) as a memorandum of recorded recollections,[4] under Rule 304(b)(2) as a statement of recent perception and under Rule 804(b)(4) as statements against interest.[5] In addition, both exhibits are admissible in the Court's discretion under Rule 803(24) and 804(b)(6) as "having comparable circumstantial guarantees of trustworthiness."[6] In this connection, I find that these notes were material, trustworthy and more probative than any other evidence which Plaintiff could procure through reasonable efforts concerning the January, 1984, meeting and the subsequent telephone calls between representatives of Southern Bancorporation and First Union.[7]

SUFFICIENCY OF EVIDENCE AS TO S.E.C. RULE 10b-5

There was evidence that Plaintiff and her husband owned the precise amount of stock which First Union sought to purchase. Southern Bancorporation's Chief Executive Officer testified that Plaintiff's husband had previously stated that if he were ever terminated, he would sell his stock. There was evidence that the January, 1984, meeting and its resulting "pinning" agreement were concealed from him even though he was a member of the Executive Committee and the Board of Directors.

Southern Bancorporation notified First Union of its approval of their intended stock purchase on February 2, 1984 [Plaintiff's Exhibit #3A]. A representative of Southern Bancorporation admitted that he deliberately lied to Plaintiff's

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[3] *See,* Annotation: 75 A.L.R. Fed. 170 (1985).

[4] *See, U. S. v. Ray,* 768 F.2d 991 (8th Cir. 1985).

[5] *See, U. S. v. Brainard,* 690 F.2d 1117, 1123-25 (4th Cir. 1982).

[6] *See, Cooperweld Steel Co. v. Demag-Mannesmann-Bohler,* 578 F.2d 953, 963-64 (3rd Cir. 1978); *U. S. v. Howard,* 774 F.2d 838, 845-46 (7th Cir. 1985); *U. S. v. Carlson,* 547 F.2d 1346 (8th Cir. 1976); and *Turbyfell v. International Harvester,* 486 F.Supp. 232 (E.D.Mich. 1980). *See, also,* Annotations in 36 A.L.R. Fed. 742 (1978) and 51 A.L.R.4th 999 (1987).

[7] *See, Cooperweld Steel, supra Note 6,* 578 F.2d 964, Headnotes 9 and 10, and *U. S. v. Howard, supra Note 6,* 774 F.2d 846.

husband concerning the purpose of the meeting, only four days later, at which he was precipitously fired. Then, only two days after his termination, Southern Bancorporation's Chief Executive Officer wrote to Plaintiff's husband stating that, unless he agreed to sell his stock, all of his benefits would be terminated [Plaintiff's Exhibit #7].

There was evidence that a broker, calling on behalf of First Union, misrepresented the identity of his principal. There was evidence that First Union's identity as the actual purchaser was concealed until Plaintiff's husband had committed to the $18.00 per share sales price. In addition, there was evidence that Southern Bancorporation knew, but did not disclose to Plaintiff or her husband, the fact that a fellow board member wanted to purchase their stock. From the evidence, the jury could have concluded that Southern Bancorporation discouraged him from contacting the Taylors.

In their argument on this issue, the Defendants sought to isolate each claimed act of misrepresentation or disclosure. However, the jury could well have concluded that Defendants' acts of coercion, misrepresentation and non-disclosure were all part of a single scheme to coerce, manipulate and defraud Plaintiff and her husband into a sale of their stock to First Union at a price dictated by the Defendants.

In *Sante Fe Industries v. Green*,[8] the Supreme Court stated that where a plaintiff bases his or her claim for violation of Rule 10b-5 on manipulative devices and schemes not primarily involving misrepresentation and non-disclosure, the plaintiff must also show that there was some element of deception on the part of the defendant used to mislead the plaintiff. Here, there was certainly sufficient evidence of deception by the Defendants to satisfy this rule.

BREACH OF FIDUCIARY DUTY

Plaintiff and her husband were shareholders in Southern Bancorporation and, under South Carolina law, officers

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[8] 430 U.S. 462, 97 S.Ct. 1292, 51 L.Ed.2d 480 (1977).

and directors of a corporation clearly have a fiduciary duty to the corporation's shareholders.[9] There was evidence from which the jury could have concluded that Southern Bancorporation's officers and directors breached their fiduciary duty to Plaintiff and her husband. Under the Doctrine of Respondeat Superior, Southern Bancorporation would have been responsible for the breach of fiduciary duty of its officers and directors committed within the course of their agency relationship.[10] In addition, I have concluded that the Supreme Court of South Carolina would hold that, under South Carolina law, the corporation itself has a fiduciary duty to its shareholders.[11] Therefore, Southern Bancorporation's position on this point is without merit.

As to First Union, Plaintiff's claim for breach of fiduciary duty was based upon her claim that First Union conspired with Southern Bancorporation to breach Southern Bancorporation's fiduciary duty to the Plaintiff. There was ample evidence to support the jury's conclusion that such a conspiracy existed.

The remaining grounds argued in support of Defendants' motion are without merit and the motion is therefore denied.

G. Ross Anderson, Jr.
United States District Judge

Greenville, South Carolina
December 28, 1987

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[9] *See, e.g., South Carolina Code,* § 33-15-150.

[10] *See, e.g., Diamond v. Oreamuno,* 24 N.Y.2d 494, 301 N.Y.Supp.2d 78, 248 N.E.2d 910 (1969).

[11] *See, e.g., Kohler v. Kohler,* 319 F.2d 634, 638, 7 A.L.R.3d 486 (7th Cir. 1963); *Wright v. Bayly Corp.,* 41 Colo.App. 313, 587 P.2d 799 (1978); and *Yeaman v. Galveston City Co.,* 106 Tex. 389, 167 S.W. 710, 723 (1914).

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 88-2503

Patricia B. Taylor, Plaintiff-Appellee,

versus

First Union Corporation of
South Carolina, et al, Defendants-Appellants.

On Petition for Rehearing with Suggestion
for Rehearing in Banc

The appellee's petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of this Court or the panel requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied.

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

Entered at the direction of Judge Wilkinson, with the concurrence of Judge Russell and Judge Niemeyer, United States District Judge sitting by designation.

For the Court
John M. Greacen
CLERK

Supreme Court, U.S.
FILED
FEB 14 1989
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-1216

In The

Supreme Court of the United States

October Term, 1988

PATRICIA B. TAYLOR,

Petitioner,

v.

FIRST UNION CORPORATION OF SOUTH CAROLINA AND FIRST UNION CORPORATION,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF IN OPPOSITION

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February 14, 1989

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QUESTIONS PRESENTED

1. Does Rule 10b-5 require a nexus between the fraud and the sale of securities?

2. Does either a rejected suggestion of a possible future merger or discussions that do not rise to the level of preliminary merger negotiations constitute a material fact under Rule 10b-5?

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First Union Corporation of South Carolina, formerly Southern Bancorporation ("Southern"), and First Union Corporation ("First Union")* submit this response to the Petition for a Writ of Certiorari received on January 18, 1989.

STATEMENT OF THE CASE

Unlike the Petition, the Fourth Circuit's opinion contains a succinct and unbiased statement of the facts. Respondents will not restate them here.

The Fourth Circuit held that:

1. First Union's and Southern's silence about discussions that occurred at their January 11, 1984, meeting was not misleading;

2. Any discussions that occurred during the meeting were not material and did not require disclosure;

3. Any conduct which allegedly was fraudulent or deceptive was not "in connection with" the purchase or sale of a security; and

4. Petitioner failed to prove a claim for breach of fiduciary duty under South Carolina law.

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* The respondents are First Union Corporation and its wholly-owned subsidiary First Union Corporation of South Carolina. They have no other parent companies, subsidiaries, or affiliates other than wholly-owned subsidiaries.

The Fourth Circuit reversed, ordering that judgment be entered in respondents' favor. *Taylor v. First Union Corp.*, 857 F.2d 240 (4th Cir. 1988).

REASONS WHY THE WRIT SHOULD BE DENIED

No basis for granting a writ of certiorari exists here. Petitioner cites no case decided in any circuit that even appears to conflict with the Fourth Circuit's ruling. The Fourth Circuit followed to the letter the precedents of this Court, including *Basic, Inc. v. Levinson*, 108 S. Ct. 978 (1988). Petitioner simply disagrees with the Fourth Circuit's conclusion that the evidence did not justify submitting this case to the jury.

I. THE FOURTH CIRCUIT'S HOLDING THAT RULE 10b-5 REQUIRES A NEXUS BETWEEN THE FRAUD AND THE SALE OF SECURITIES IS CONSISTENT WITH THE DECISIONS OF THIS COURT AND OF OTHER CIRCUITS.

In order for liability to be imposed under Rule 10b-5(3), there must be evidence that the defendant engaged in activities that "operate as a fraud or deceit . . . in connection with the purchase or sale of any security." Petitioner contends that the Fourth Circuit's reading of the "in connection with" requirement conflicts with decisions of this Court and other circuits. This contention has no merit.

The court of appeals correctly held that the evidence which petitioner contends met the "in connection with" requirement related not to the purchase or sale of any

security, but to Southern's firing of Taylor, her husband. Taylor expressed his desire to sell his stock at the moment he was fired. He never altered that decision. The only negotiations about Taylor's stock related to its price, not whether he wished to sell. Taylor, with full knowledge that First Union was the buyer, with full knowledge that the price of the stock could increase in the event of interstate banking, and against the advice of his attorney, sold his and petitioner's stock. The "fraud" of which petitioner complains was the pretext by which Southern encouraged Taylor to attend the meeting where he was fired, and the alleged threat to revoke his disability benefits. She cannot, and does not, claim that the firing itself was unjustified or fraudulent. So even if Taylor's discharge was "in connection with" the stock sale, it was not "fraudulent."

Petitioner contends four cases are "at odds with" the decision of the Fourth Circuit. Petition at 7-8. However, each case she cites required a nexus between the fraud and the sale of a security. Furthermore, each court found no Rule 10b-5 violation. Those decisions are consistent with the Fourth Circuit's opinion.

In *Rochelle v. Marine Midland Grace Trust Co.*, 535 F.2d 523 (9th Cir. 1976), the court affirmed the dismissal of a Rule 10b-5 claim for failure of the plaintiff to satisfy the "in connection with" requirement. Petitioner cites language from this case relating to the scope of the "in connection with" requirement, but fails to inform the Court that the quoted paragraph goes on to state:

> No comprehensive definition of these tactile concepts is practicable; rather each alleged scheme must be examined in its own context to determine whether

> the deception . . . caused injury to persons suing who bought or sold securities . . . .

535 F.2d at 529. The only other circuit court decision cited by petitioner, *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974), states that determining whether the "in connection with" requirement has been met should be done on a case-by-case basis. In the present case, the Fourth Circuit examined the alleged scheme in its own context, and found no connection with the sale of a security.

Petitioner then contends two district court cases conflict with the Fourth Circuit. Even if these cases are in conflict, which they are not, this would not merit certiorari. The Fourth Circuit holding that no fraud occurred "in connection with" the sale of a security does not conflict with the law of any other circuit.

II. THE FOURTH CIRCUIT CORRECTLY CONCLUDED THAT THERE WAS INSUFFICIENT EVIDENCE OF A CONSPIRACY.

Petitioner asserts that the Fourth Circuit failed to interpret correctly her "conspiracy" evidence. Petitioner makes no argument that the Fourth Circuit's decision in any way conflicts with decisions in other circuits or with any decision of this Court. Rather, she only complains that the Fourth Circuit ruled wrongly on the quantum of evidence necessary to support a conspiracy claim. Thus petitioner's argument, even if meritorious, would not warrant consideration on certiorari.

Furthermore, the argument is specious because petitioner relies on "facts" which are taken out of context,

mischaracterized, or both. Petitioner implies that notes of a First Union executive mentioning an "agreement in principle" and an "agreement to merge" were taken at the January 1984 meeting and show that First Union and Southern reached such an agreement. Petitioner ignores the fact that these notes were made long before the meeting, and simply listed alternatives available when First Union was considering investing in southeastern banks.

Similarly, petitioner claims that Taylor's termination was planned to get him to sell his stock to First Union. This has no support in the record. The uncontroverted evidence is that Southern's management learned of the impending resignation of Taylor's entire management team. This intensified Southern's mounting concerns about Taylor's bizarre behavior and management failures, and led to the decision to terminate his employment. Petitioner argues that Southern fired Taylor to make him sell his stock. Taylor was under no obligation to sell, and offered to do so on his own initiative.

Even if evidence of a conspiracy had been presented, this evidentiary issue fails to meet the standard for review on certiorari.

III. THE FOURTH CIRCUIT STRICTLY FOLLOWED *BASIC, INC. V. LEVINSON.*

Petitioner asserts that the Fourth Circuit's opinion is irreconcilable with *Basic, Inc. v. Levinson,* 108 S. Ct. 978 (1988). In fact, the Fourth Circuit followed *Basic* to the letter.

Basic requires a fact specific inquiry to determine whether preliminary merger negotiations are material

and must be disclosed. The Fourth Circuit conducted such an inquiry and found none of the factors listed in *Basic*. Neither respondent had previously denied the possibility of a future merger. On the contrary, Southern had publicly identified itself as a potential acquisition target should interstate banking become legal. As is pointed out by the Fourth Circuit, the respondents' discussion prior to petitioner's sale of her stock resulted in no more than "a vague 'agreement' to establish a relationship." *Taylor v. First Union Corp.*, 857 F.2d 240, 244 (4th Cir. 1988). There were no agreements as to price or structure, no board resolutions, no actual negotiations, and no instructions to investment bankers to facilitate a merger. Furthermore, at the time of the 1984 discussion and First Union's purchase of petitioner's stock, no merger was possible because this Court had yet to rule on the constitutionality of interstate banking. *Id.*

As the Fourth Circuit stated, to require disclosure of such tentative discussions "would result in endless and bewildering guesses as to the need for disclosure, operate as a deterrent to the legitimate conduct of corporate operations, and threaten to 'bury the shareholders in an avalanche of trivial information.' " *Id.* at 245.

CONCLUSION

The questions raised in the Petition for a Writ of Certiorari do not rise to the level of substance and importance worthy of this Court's attention. The issues satisfy none of the requirements of Rule 17 of this Court. The

Petition for a Writ of Certiorari should, therefore, be denied.

Respectfully Submitted,

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